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In the

Supreme Court of the United States

OCTOBER TERM, 1966.

No. [redacted] 208

CHICAGO CUTTER KARCHER, INC.,

Petitioner,

vs.

CHARLES D. MALEY, Trustee of LORDS, INC., Bankrupt,

Respondent.

MOTION OF CONSOLIDATED MILLINERY COMPANY FOR LEAVE TO FILE A BRIEF, AMICUS CURIAE, IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

AFFIDAVIT IN SUPPORT OF MOTION AND BRIEF

BRIEF OF CONSOLIDATED MILLINERY COMPANY, AMICUS CURIAE

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Consolidated Millinery Company respectfully moves this Court, pursuant to Rule 42 of this Court, for leave to file the attached brief, *amicus curiae,* in support of the petition for a Writ of Certiorari. The respondent has refused to consent to the filing of such a brief. The purpose of the brief is to bring to the attention of the Court important factual matters concerning leasing operations in department stores not presented to the court below. An affidavit setting forth these facts is hereto attached.

The petition seeks review of a decision of the Circuit Court of Appeals for the Seventh Circuit which, if

allowed to stand, will seriously injure many small and independent department stores and many companies engaged in the business of leasing departments in department stores.

Consolidated Millinery Company is engaged exclusively in the business of leasing departments in department stores. It operates millinery departments in over 300 stores. Many of these departments are operated pursuant to leases containing trust provisions similar to the one in question here. Several stores with which Consolidated Millinery Company has such leases have become insolvent. Consolidated Millinery Company has a substantial interest in the determination of this question because the decision of this case will necessarily affect its right under these leases.

Leased departments have become a major factor in modern retail merchandising. The latest study indicates that leased departments account for approximately 10% of all sales in department stores. More than 24% of the stores surveyed leased their shoe departments and over 43% leased their millinery departments. The availability of lessees is especially important to small or marginal stores who operate independently. Often these stores need to establish new departments in order to remain competitive with larger stores. Many of these stores, however, cannot successfully expand on their own because of problems in financing or because a new department would require special experience, equipment, or trained personnel. The only way for a store in this position to remain competitive is to find a lessee to put in the new department for it.

A lessee is especially vulnerable if its lessor becomes insolvent. The lessor may have up to 46 days receipts from the leased department in its possession. The lessee

at the same time incurs expenses not incurred by a general creditor.

The only way a lessee can protect itself is to provide, in the lease, for a trust arrangement such as the one at bar. The decision below holds that any such trust arrangement is void if the lessee's funds are commingled with those of the lessor. Credit sales form a large part of retail sales. Store credit extended to customers by leased departments is required to make possible essential integration of the leased operation. This fact and the cost and inconvenience of treating cash and credit sales separately makes it practically impossible to separate the funds of the leased department. In fact the decision below destroys all possibility of any effective trust agreement.

Besides causing a hardship to lessees who have been operating in good faith pursuant to trust arrangements, the decision below will greatly increase the difficulty small stores will have in finding the lessees they need. Prospective lessees will be less willing to contract with small stores because they cannot protect themselves from the risk involved. These stores will have a much harder time maintaining or improving their competitive position because it will be more difficult for them to add the new departments necessary to attract new customers or keep old ones.

Finally, the decision below provides a windfall to the general creditors. There are several readily available sources from which these creditors could, in the exercise of due care, have discovered which departments the bankrupt leased. The general creditors knew or should have known that they could look neither to the merchandise in these departments nor the receipts therefrom if the store became insolvent.

It is submitted that the above facts should be taken into account by this Court when considering the petition for a writ of certiorari. The effect of the decision of the court below on department leasing cannot be over-emphasized. The probability of serious harm resulting to lessees and lessors should not be overlooked by this Court.

Respectfully submitted,

.....

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Dated at Chicago, Illinois, August 26, 1966.

AFFIDAVIT IN SUPPORT OF MOTION AND BRIEF

State of Illinois }
County of Cook } SS.

W. Alvin Wineberg, being first duly sworn on oath, deposes and says:

(1) I am the President of the movant herein, Consolidated Millinery Company, an Illinois corporation.

(2) Consolidated Millinery Company is engaged exclusively in the business of leasing millinery departments in various department and specialty stores. Consolidated Millinery Company leases over 300 such departments in 48 states, with sales in excess of $20,000,000.00 a year.

(3) The leases between Consolidated Millinery Company and the various stores usually provide that all receipts from the leased department are to be turned over to the store. The store deducts its rent and various other charges and then returns the remainder to Consolidated Millinery Company on the 15th of the following month. All credit sales must be approved by the store and are handled in the same manner as credit sales at store operated departments. Many of these leases provide that the lessor is to hold the said receipts in trust for the lessee, but do not require separate bank accounts. None of the leases require segregation of funds.

(4) Several stores with whom Consolidated Millinery Company has leases containing such trust provisions, have become insolvent.

(5) I have been engaged in the field of leasing departments in stores for over 30 years, and am intimately familiar with this aspect of retail merchandising.

(6) Consolidated Millinery Company always attempts to secure a trust provision in any lease it signs with a small or marginal store. Depending on the particular store, Consolidated Millinery Company may refuse to execute a lease unless it contains such a provision.

(7) Approximately 40% to 60% of the sales made in departments leased by Consolidated Millinery Company are credit sales.

(8) The publication *Leased Departments: Rates, Policies, and Expenses in Department and Specialty Stores,* published by the Controllers' Congress of the National Retail Merchants Association, 100 West 31st Street, New York, New York, (1965), contains the following information:

(a) 164 Department and specialty stores, varying from $1,000,000.00 to $20,000,000.00 in annual sales were surveyed. (p. 6);

(b) The department stores leased 10% of their departments (median) (p. 6);

(c) The leased department accounted for 10% of the sales in main department stores (median) (p. 6);

(d) Some reasons given by small stores for leasing departments include: Leasing helps broaden a store's merchandise and service offerings; leasing provides the necessary professional management for the department; leasing allows a store to introduce new lines of merchandise or new services with a minimum capital investment risk, and leasing allows a store to expand more rapidly than its own capital permits. (p. 7);

(e) The reporting stores said the lessee paid the following expenses in connection with the leased department: Salaries of sales personnel, 100%; prepara-

tion of payroll tax returns, 91%; advertising space, all but one store; advertising mats, cuts, etc., 96%; license fees, 90%; cash shortages, 74%; customer claims and damages, 91%; Workmen's Compensation insurance, 93%; fidelity bond, 76%; public liability insurance, 67.5%; products liability insurance, 76%; special equipment, 84%; salaries of floor cashiers and wrappers, receiving and marking salaries, advertising heads and tails, publicizing a new leased department, office supplies, delivery by an outside agency, fire insurance on fixtures, and depreciation on fixtures and equipment, all over 50%. (pp. 32-36).

(f) 75.4% of the stores reported leasing their beauty salon, 43.4%, their millinery department, and 25.4% their shoe department. (p. 8).

(9) The publication, "Stores" magazine for July-August (1964), also published by the National Retail Merchants Association, contains the following information:

(a) Of 200 department and specialty stores surveyed, 2% leased only service departments, 75% leased one or more merchandise departments and 23% leased no departments (p. 31);

(b) The median store leasing any departments received 9% of its sales from leased departments, and one out of four stores leasing any departments received 15% or more of its sales from those departments (pp. 31-32);

(10) The publication, *Leased Departments: Rates, Policies, and Expenses in Department and Specialty Stores,* also published by the Controllers' Congress of the National Retail Merchants Association (1958), contains the following information:

(a) 224 Department and specialty stores, ranging from 6 departments to 226, and from annual sales of

less than $1,000,000.00 to more than $20,000,000.00 were surveyed (Forward and p. 8);

(b) Leased departments in department stores accounted for 8% of all sales (median) (p. 8);

(11) The publication, *Leased Department Survey,* published by the Controllers' Congress of the National Retail Dry Goods Association, 100 West 31st Street, New York, New York (1952), contains the following information:

(a) 132 Stores, ranging from 2 departments to 240 departments and from $2,000,000.00 annual sales to $50,000,000.00 annual sales were surveyed. (p. 8);

(b) The median store did 5.2% of all sales through leased departments.

(12) The annual publications, *Sheldon's Retail Trade of the United States,* Phelon-Sheldon Publications, Inc., 32 Union Square, New York, New York, and *The Directory of Department Stores,* Department Store Guide, 2 Park Avenue, New York, New York, usually indicate which departments, if any, in a given department or specialty store, are leased. The edition of *Sheldon's* for 1963 showed which departments of Lord's, Inc., the bankrupt here, were leased and to whom, and showed that petitioner was the lessee of the shoe department.

(13) "Survey of Current Business", July, 1966, published by the U. S. Department of Commerce shows that over 30% of all department store sales are on credit (exclusive of installment sales). Credit sales in January 1966, (exclusive of installment sales) were 54.7% of total sales.

25.8% of all sales were on credit in December 1965, and 35.2% were on credit in May of that year. (pp. S-11 and S-19).

.....

W. Alvin Wineberg

Signed and sworn to before me this
26th day of August, 1966

.....

Notary Public

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BRIEF OF CONSOLIDATED MILLINERY COMPANY, AMICUS CURIAE

INTRODUCTION

Consolidated Millinery Company ("Consolidated") is a corporation, duly existing under the laws of the State of Illinois. For the last 30 years, Consolidated has engaged solely in the retail sale of women's millinery—hats, wigs, etc.—through leased departments.

Consolidated leases millinery departments in over 300 stores in 48 states. Its annual gross sales from these departments is in excess of $20,000,000.00. Typically, the leases provide: all receipts—cash and credit—from sales in these departments are turned over to the store; the

store deducts the rent and various other charges; and the balance is returned to Consolidated by the 15th day of the following month. All credit sales must be approved by the store and are handled by the store credit department in the same manner as credit sales in departments operated by the store. Many of Consolidated's leases have trust provisions similar to the trust provision in the lease to which petitioner is a party. None of these leases require segregation of funds.

The adjudication of the issues in this case are of vital importance to Consolidated and the many other companies engaged in the leasing of departments in retail stores. It is to protect its own interests and to acquaint the Court with certain information about retail leasing operations that Consolidated seeks to intervene in this petition as *amicus curiae*.

ARGUMENT.

I.

THE DECISION BELOW IGNORES THE IMPORTANCE OF DEPARTMENT LEASING IN DEPARTMENT AND SPECIALTY STORES AND WILL AFFECT A SIGNIFICANT PORTION OF TRADE AND COMMERCE.

Leased departments account for a large segment of the operations and sales volume of department and specialty stores. In 1965, a study of department leasing was published by the Controllers' Congress of the National Retail Merchants Association, entitled: *Leased Departments: Rates, Policies, and Expenses in Department and Specialty Stores* (hereafter "*Leased Departments*, 1965.") The survey included 164 Department and specialty stores, varying in annual sales from $1,000,000.00 to over $20,000,000.00. As a median, department stores leased 10% of their departments and received 10% of their sales in main stores from leased departments. (*Leased Departments*, 1965, p. 6).

Similar studies were also conducted in 1952, 1958 and 1964. The pertinent information from these studies is contained in paragraphs 9, 10 and 11, of the Affidavit, *supra*. These data establish that leased departments are a significant aspect of modern retail merchandising, and that leasing operations are increasing. In 1952 leased departments accounted for a median of 5.2% of the sales volume of the department stores surveyed. By 1957, this has risen to 8%, by 1964, 9%, and by 1965 10%.

These figures do not tell the entire story. Some departments are leased much more frequently than the

figures indicate. The 1965 report showed that 75.4% of the stores reported leasing their beauty salon, 43.4%, their millinery department, and 25.4%, their shoe department (*Leased Departments*, 1965, p. 8).

II.

REFUSAL TO GIVE EFFECT TO THE EXPLICIT TRUST PROVISIONS IN THE LEASE WILL BE DETRIMENTAL TO MANY SMALL OR MARGINAL STORES.

The decision below will inhibit the making of leases in small or marginal department stores. This will place such stores in a serious competitive disadvantage.

The trend in recent years has been to put more and more kinds of merchandise under one roof or in one area. In order to remain competitive under these circumstances, the small or marginal store must continue to expand its variety of merchandise and services. But expansion often requires expensive equipment, trained personnel, a heavy outlay of capital, intimate familiarity with special merchandising problems resulting from sudden changes in fashion or style and access to key sources of supply of merchandise. (*Leased Department*, 1965, *supra.*, p. 7). Limited resources are a bar to such essential expansion.

This dilemma can often be solved by leasing the department to someone with the necessary equipment, experience, etc. However, it may not be easy for a small or marginal store to find an acceptable lessee. A lessee considering taking over or starting a department always has to consider the increased possibility of insolvency presented by a small operation. Under the typical lease, the store will have up to 46 days' receipts of the leased de-

partment in its hands from time to time. Trust provisions similar to the one in the present case are frequently put into leases to protect the lessee from losing these receipts if the store becomes insolvent. The decision below, if left standing, will prohibit such provisions and make leasing companies very reluctant to do business with small or marginal stores. This, in turn, will result in fewer of these stores being able to retain or improve their competitive positions.

III.

THE REQUIREMENT OF THE MAJORITY BELOW THAT THE LESSEE'S FUNDS IN THE HANDS OF THE LESSOR BE SEGREGATED EFFECTIVELY PROHIBITS A TRUST ARRANGEMENT IN DEPARTMENT LEASING.

One of the essential characteristics of an effective leased operation is that it be fully integrated into the store. Integration assures retention of customer loyalty. As far as the customer is concerned, the leased operation is just another department in the store.

Integration is achieved by the lessee doing business in the name of the store and using all of the stores' services —including the credit department.

The use of the credit department is of prime importance. Integration would be defeated if a customer could not use his charge account throughout the store. Under the typical lease, credit can only be extended by the store and is guaranteed by the store.

Much of modern retail merchandishing is done on a credit basis. The July, 1966, edition of "Survey of Current Business" published by the United States Depart-

ment of Commerce, shows that well over 30% of all department store sales are credit sales. In January, 1966, department store sales in the United States totalled $1,564,000,000.00. Credit sales (exclusive of installment sales) were $855,000,000.00 or 54.7% of total sales. In the last 8 months of 1965, credit sales (exclusive of installment sales) in department stores varied from 25.8% of total sales in December to 35.2% in May. No comparable statistics are available for installment credit sales, but they would add to these percentages. ("Survey of Current Business", *supra*, pp. S-11 and S-19).

Apart from considerations of integration, customer inconvenience and increased bookkeeping, accounting, and collection expense would make it practically impossible for a lessee to carry on its own credit operation.

The court below did not take these factors into consideration in basing its decision on the admitted fact that the receipts of petitioner were commingled with funds belonging to Lords, Inc., the bankrupt. The court said:

> "The parties to a department store-leased department agreement may establish a fiduciary relationship as they did in *U. S. National Bank* v. *Blanner's Affiliated Stores, Inc.*, 3 Cir., 1935, 75 F. 2d 826, where the contract provided for the funds collected to be kept in a separate account for the lessee. The parties have not done that here." (Petition for writ of certiorari, p. 19).

The requirements of the court below could be met only if the store placed a cash amount equal to the credit sales of its leased departments into a separate account as fast as those credit sales were made. This would visit undue hardship on the store. As the month progressed, it

would find larger and larger amounts of its working capital tied up in the special accounts, non-recoverable until after the end of the month when the store's customers paid their bills. Further, this hardship would be visited only on those stores least able to absorb it—the small or marginal stores which can attract acceptable lessees only by agreeing to some kind of effective trust arrangement. The effect of the decision below is to make any such trust arrangement impossible, and therefore to greatly diminish the competitive abilities of these smaller stores.

IV.

THE RULING OF THE COURT BELOW FAILS ENTIRELY TO TAKE THE SPECIAL VULNERABILITY OF A LESSEE INTO ACCOUNT.

The effect of the ruling below is to prevent a lessee from becoming anything other than a general creditor if the lessor-store fails. But the lessee's risks are much greater than those of a general creditor who risks only the price of the goods sold to the store on credit. If the store goes bankrupt, the general creditor loses only some part of his investment. Under the decision below, the lessee will lose not only part of the cost of the goods he has brought into the store but, also advances for additional expenses not borne by the general creditor.

Leased Departments, 1965, *(supra)* shows that the greatest percentage of lessees bear such expenses as salaries of sales personnel, preparation of tax returns, advertising, license fees, cash shortages, customer claims and damages, insurance of various kinds, special equipment, and so forth. The exact figures reported are contained in sub-paragraph 8(e) of the Affidavit, *supra*.

All of these expenses are in addition to the rent the lessee must pay. Most are expenses which the lessee must bear whether or not the lessor is able to meet its obligations at the end of any given accounting period.

Another major difference between lessees and general creditors should be noted. Most suppliers sell things to many stores, so their entire business is usually not threatened if one goes bankrupt. A lessee's entire business is tied up in that store. Because it is integrated into the store, it has built up no customer loyalty of its own. Further, the store may have a substantial sum of the lessee's money in its hands. The lessee loses its business, and, under the decision below, its receipts if the store fails.

The only way a lessee can protect itself from a blow of this kind is to include a trust agreement like the one in question in the lease. The opinion below effectively prevents this.

V.

THE DECISION OF THE COURT BELOW OPERATES AS A WINDFALL TO THE GENERAL CREDITORS.

The general creditors of the bankrupt either knew, or in the exercise of reasonable diligence, should have known that the bankrupt had leased the shoe department to petitioner. At least two publications, generally available to companies in the merchandising field, indicate which, if any, departments in a store are leased. These publications are: *Sheldon's Retail Trade of the United States*, Phelon-Sheldon Publications, Inc., 32 Union Square, New York, New York; and *The Directory of Department Stores*, Department Store Guide, 2 Park Avenue, New York, New York. The 1963 edition of *Sheldon's* shows

that the bankrupt leased four departments and to whom they were leased.

The effect of the decision below is to give creditors a pro-rata share of petitioner's funds in the hands of the bankrupt. This is windfall because they could not reasonsably have expected to look to receipts from any leased department if the store became insolvent.

CONCLUSION

Department leasing in department and specialty stores is an important aspect of modern merchandising. It is especially important to stores which are small, marginal, or in temporary financial difficulties. The decision of the court below will have a serious adverse impact on this important part of our retail economy and should be reviewed.

Respectfully submitted,

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August 26, 1966